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UNCLAS SECTION 01 OF 03 LAGOS 000302

SENSITIVE
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DOE FOR GPERSON, CHAYLOCK

E.O. 12958: N/A
TAGS: ENRG PGOV NI
SUBJECT: NIGERIA: LOCAL INVESTOR SAYS POWER PROJECTS THAT
CONTROL DISTRIBUTION AND COLLECTION OF FEES ARE MOST VIABLE

REF: A. LAGOS 122
¶B. ABUJA 840
¶C. 07 LAGOS 750

¶1. (SBU) Summary: In a June 30 meeting with Resources Officer, Adewale Audifferen, former Managing Director of General Electric Nigeria, now Vice President for Power at Global Energy Nigeria (GE), said independent power projects (IPPs) like the Geometric Plant being built in Abia State are the most viable because they are vertically integrated, controlling distribution and collection of user fees. Chinese construction in Ondo and Ogun State's plants was shoddy; the Government of Nigeria (GON) contracted GE to complete the projects. High import taxes on electrical equipment hurt Nigeria's effort to improve power generation capacity. Natural gas remains the best choice for fueling Nigeria's electric power. End Summary

Controlling Distribution Key to Revenue Stream

¶2. (SBU) Resources Officer met June 30 with Adewale Audifferen who said the most viable and sustainable power projects will be structured like the Geometric Power Ltd power plant's captive power model currently under construction in Abia state. That project is a stand alone, off-grid power project with Geometric building everything from gas pipelines to the power plant, transmission lines, and distribution networks. It is estimated that the transmission lines will be in place by June 2009; the plant is expected to be completed by November 2009. By employing the captive power model of vertically integrating and particularly by controlling distribution and collection of payments, Geometric will be able to guarantee a revenue stream from the sale of electricity. He estimates Geometric will receive an average of 17 naira (USD 0.14) per kilowatt hour, double what it would get from selling under Power Purchase Agreement (PPA) to the national grid.

¶3. (SBU) In contrast, Independent Power Producers (IPPs) that sell to Nigeria's quasi-state owned Power Holding Company of Nigeria (PHCN), in addition to facing a lower tariff, must struggle with the not inconsequential burden of actually getting paid. (Note: U.S. company AES Barge Nigeria, the only operating IPP in Nigeria, is seeking arbitration in a dispute with PHCN over the terms and conditions of its PPA. Payments on its existing PPA are perpetually in arrears. End

Note) In Audifferen's opinion, while Nigeria's newly announced Multi-Year Tariff Order is a significant improvement over the old electricity tariff structure (ref A), it falls just short of what is necessary to make independent power projects economically attractive to many investors, especially foreign investors. Still, he said it was a significant step in the right direction.

GON Growing Leery of Chinese Power Plants

¶4. (SBU) Audifferen saw most of the financing for power projects coming from local banks, which, he noted, are awash with capital. Nigerian banks are able to offer financing at much more competitive rates than they currently do, but he said they lack technical expertise to develop sound project financing. (Note: The AES Barge Nigeria finance manager has said Nigerian banks are "knocking down the door" to offer financing to AES. End Note) Financing from Chinese or Indian sources was less likely; Audifferen says most Chinese capital flowing into Nigeria is destined for the real estate sector, which is less technically complex and offers a quicker payoff.

¶5. (SBU) On Chinese participation in power generation construction, Audifferen was notably dismissive. He recounted how Chinese contractors built two power plants for the GON, the Papalanto Thermal Power Station in Ogun State and Omotosho Thermal Power Station in Ondo State. Both plants, he said, suffered from cost overruns and commissioning delays. According to Audifferen, the GON

ordered the Chinese contractors to bring in General Electric to help complete the commissioning. GE engineers were shocked at the poor quality of construction and the failure to comply with industry safety standards. Overall, Audifferen thought the GON was growing leery of Chinese participation in complex infrastructure projects.

Import Taxes Hurt Power Plant Construction

¶6. (SBU) One of the biggest obstacles to private sector investment in the electricity sector was Nigeria's onerous and "self-defeating" import taxes. Despite the obvious need to expand its generating capacity, Nigeria continues to levy steep duties on the importation of electrical equipment and associated raw and semi-finished materials like cement, flat-rolled steel, and wire cables. Increased construction costs require larger loans, requiring increased financial payments or debt structures with longer tenures and accordingly higher interest rates, Audifferen said. Including financing, a Nigerian power project costs around USD 4 million per megawatt.

Gas Still Power Generation's Best Choice

¶7. (SBU) Audifferen lamented that lack of coordination between electricity and natural gas planners. Like many of our contacts, he noted that access to natural gas is the most significant operational impediment to power generation. While generally supportive of Nigeria's gas master plan, Audifferen viewed the natural gas pricing policy (ref B, C) as unworkable and unlikely to make new gas available for power customers because of the unreasonably low gas price set by the GON. Audifferen was disappointed in the roadshow put on by the Nigerian National Petroleum Corporation (NNPC) to attract new natural gas sector investors (held April in Abuja and May in Houston, TX). NNPC, in his opinion, failed to properly target large international institutional investors. When asked about alternatives to natural gas, Audifferen dismissed coal as too expensive in the short term, saying the mines are not yet developed and the lack of a robust road and rail infrastructure in Nigeria makes shipping coal

prohibitively expensive.

¶8. (SBU) Audifferen noted that Oando Plc, a mid and downstream petroleum company, was taking advantage of its ownership of a natural gas pipeline in Lagos State to expand into the electricity sector. According to Audifferen the company has moved aggressively to offer to build power plants for companies seeking gas purchase agreements. The international oil companies, which also produce natural gas, have no interest in getting into the power plant building business in Nigeria.

¶9. (U) Audifferen's company, Global Energy Nigeria, is a small, privately held company lead by Nigerians with international experience in the oil, natural gas, and electricity industries. Besides its interests in electricity, the company owns seven small Nigerian oilfields and is a minority partner in Enviro Africa, a company working in the carbon credit markets.

¶10. (SBU) Comment: Like any good businessman Audifferen saw the myriad problems as an opportunity to make money. Although he noted the difficulty of doing business in the sector, Audifferen and his company are clearly bullish on the prospects in the gas sector. He epitomizes an important element of doing business in Nigeria; namely, it helps to actually be in Nigeria. Although investors, and American investors in particular, cannot only rely on analysts and bankers who reside in London, New York, and Johannesburg, flying in to Abuja or Lagos only on occasion, to provide a picture of the situation on the ground. Opportunities exist, but the Nigerian market, is too opaque to permit investing at arm's length, but no noted best business practices and sanctity of contract remain real issues here. End Comment.

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